

## Brazilian sanitation companies squeezed as government delays decrees on new law

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**Strategic Considerations:** The Brazilian Congress approved the new regulatory framework for water and sanitation, with expectations of generating as much as USD 130bn in investments. President Jair Bolsonaro signed the new regulatory framework into law in mid-July, with several vetoes that Congress still hasn't reviewed. Since then the sector has been waiting for the publication of important decrees, including the one that will set out the economic and financial conditions companies have to meet to make the required investments. That decree could determine whether state-owned companies will be able to continue operating.

- The government is expected to publish decrees after Congress reviews vetoes
- Congress is likely to vote on vetoes only after the election of heads of lower and upper houses

President Jair Bolsonaro signed the new regulatory framework for water and sanitation into law in mid-July, with some vetoes. Since then, state-owned operators have faced uncertainty while they wait for a decree that will determine the economic and financial conditions companies must meet to get financing for investments and achieve the goal of universal coverage by 2033, said Fernando Vernalha, from Vernalha Pereira Advogados.

The Bolsonaro administration had 90 days after the new regulatory framework was signed in July to publish the decree, according to the new law, but has not done so. The government has been indicating that it will wait until Congress votes on Bolsonaro's vetoes, said Vernalha and Rodrigo Bertocelli, an attorney with Felsberg Advogados specializing in infrastructure and sanitation.

"This is the most important decree because it will determine which state-owned companies have real conditions to continue operating or have to leave the game," said Vernalha. These companies need to wait for the rules in the decree to prove they have the capacity to meet the universal-coverage targets, either with their own cash or via loans and other financing, said Vernalha.

Meanwhile, although Congress had 30 days to vote on the vetoes after the president signed the bill, it has been postponing the vote while legislators focused on approving emergency laws for the coronavirus pandemic, as reported.

Now the vetoes are unlikely to be reviewed before the early-February elections of the heads of both houses of Congress, said a source from the Senate. Also, these changes in Congress will likely weigh on how lawmakers vote on the presidential vetoes, the same source added.

If the government keeps delaying the publication of the decree, it will reduce the window companies have to get alternative funding sources to finance investments, said Vernalha.

According to the new regulatory framework, state-owned companies operating concessions have until 31 March 2022 to reflect the law's water and sanitation targets in their contracts. Because most state-owned companies have a limited capacity to invest, they will have to provide information about alternative financing sources to make the planned investments feasible, said Vernalha.

Once the decree is published, if the state-owned companies don't meet the conditions to finance investments, there will be a need for more water and sanitation auctions, opening more opportunities for private investment, said Teresa Venaglia, BRK Ambiental CEO, during a Credit Suisse online conference on Latin American Investment.

The biggest players in the sector, such as the state-owned companies Sabesp, from the state of Sao Paulo, and Copasa, from Minas Gerais, have already announced increases of around 20% to 30% in capex to meet the targets foreseen in the law for 2033, said Fitch Ratings Director Gustavo Mueller. However, several state-owned companies risk losing their contracts depending on the strictness of the conditions of the delayed decree, he added.

The sector will need between BRL 500bn and BRL 700bn (USD 93bn and USD 139bn at today's exchange rate) in investments to reach the universal-coverage target by 2033, as reported.

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Region:

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Country:

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Companies/Issuers:

**Companhia de Saneamento Basico do Estado de Sao Paulo - Sabesp (BZ:SBSP3)**

**Agea Saneamento e Participacoes S.A.**

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Water and sanitation projects will require as much as BRL 50bn-BRL 60bn (USD 9bn-USD 11bn) in investments per year to reach this target, and the sector is expected to pursue a wide range of financing sources besides the development banks, similar to what was seen a few years ago in the power sector, said Felipe Pinto, partner at the local fund Patria Investimentos, during the same online conference.

by Fabiola Gomes, Sao Paulo

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